



Policy Note

2017 / 1

INEQUALITY UPDATE: WHO GAINS WHEN INCOME GROWS?

PAVLINA R. TCHERNEVA

Growth in the United States increasingly brings income inequality. A striking deterioration in this trend has occurred since the 1980s, when economic recoveries began delivering the vast majority of income growth to the wealthiest US households. This policy note updates my original inequality chart (Figure 1) with the latest data. (For earlier discussions, see Irwin 2014 and Tcherneva 2014a, 2014b.)

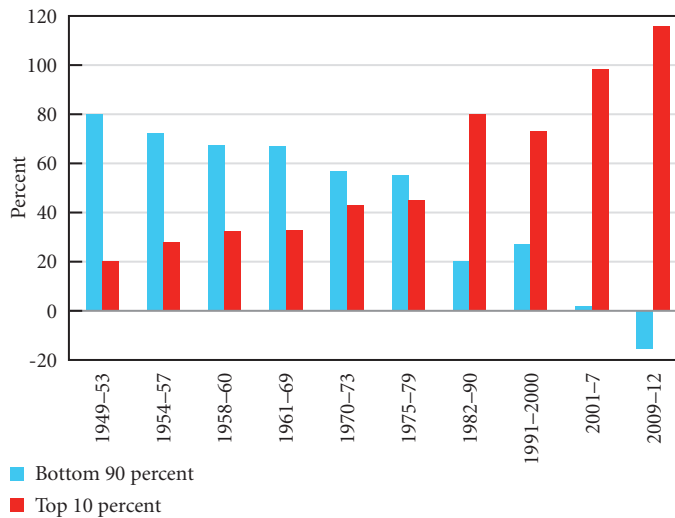
The chart illustrates that with every postwar expansion, as the economy grew, the bottom 90 percent of households received a smaller and smaller share of that growth. Even though their share was falling, the majority of families still captured the majority of the income growth until the '70s. Starting in the '80s, the trend reverses sharply: as the economy recovers from recessions, the lion's share of income growth goes to the wealthiest 10 percent of families. Notably, the entire 2001–7 recovery produced almost no income growth for the bottom 90 percent of households and, in the first years of recovery following the 2008 great financial crisis, their incomes kept falling during the expansion, delivering all benefits from growth to the wealthiest 10 percent. A similar trend is observed when one considers the bottom 99 percent and top 1 percent of households (for details, as well as complete business cycle data, see Tcherneva 2015).

Research Associate PAVLINA R. TCHERNEVA is associate professor of economics and director of the economics program at Bard College.

The Levy Economics Institute is publishing this research with the conviction that it is a constructive and positive contribution to the discussion on relevant policy issues. Neither the Institute's Board of Governors nor its advisers necessarily endorse any proposal made by the author.

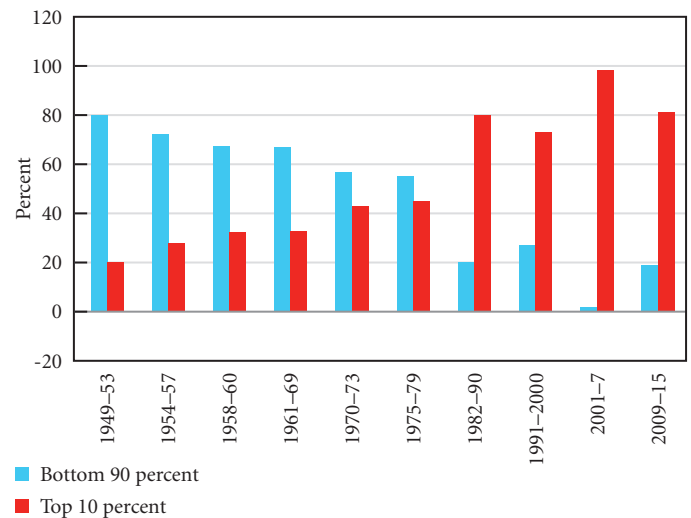
Copyright © 2017 Levy Economics Institute of Bard College ISSN 2166-028X

Figure 1 Households' Share of Average Income Growth: 1949–2012 Expansions (including capital gains)



Sources: Author's calculations based on Piketty/Saez data and NBER

Figure 2 Households' Share of Average Income Growth: 1949–2015 Expansions (including capital gains)



Sources: Author's calculations based on Piketty/Saez data and NBER

The following figures update this analysis with the latest data (up to 2015) by looking at the distribution of average income growth (with and without capital gains) between the bottom 90 percent and top 10 percent of households, and between the bottom 99 percent and top 1 percent of households.¹

I find that little has changed when considering the distribution of average income growth between the bottom 90 percent and top 10 percent of families, with or without capital gains (Figures 2 and 3).

One difference is that average real income for the bottom 90 percent of households is no longer shrinking. In 2014 and 2015, it finally began to recover. Nevertheless, these families still capture a historically small proportion of that growth—only between 18 percent and 22 percent. The growing economy continues to deliver the most benefits to the wealthiest families.

Since the top 10 percent of households is a rather heterogeneous group (see Table 1), I consider the distribution of average income growth between the bottom 99 percent and top 1 percent (Figures 4 and 5).

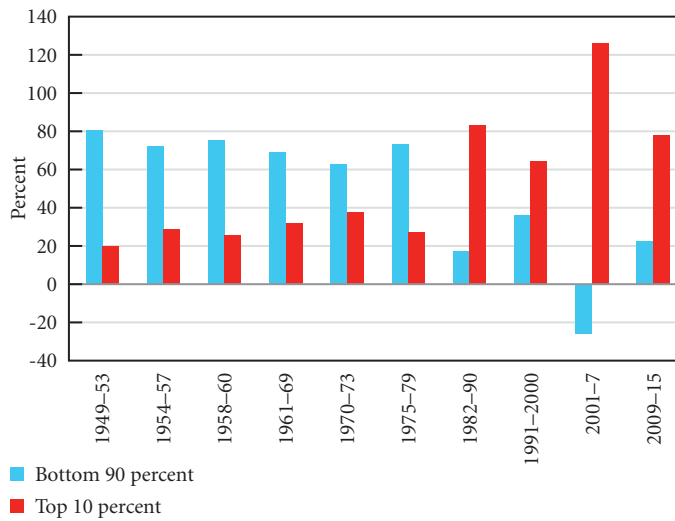
Income varies greatly in this group. The average income for the top 0.01 percent of income earners is more than 100 times higher than that for the entire top 10 percent. Additionally, capital gains income is highly concentrated at the very top: it makes up 22 percent of average real income for the top 1 percent of households and only 3 percent (not shown) for the bottom 99 percent. But capital gains constitute 40 percent of average real income for the top 0.01 percent. Because data are collected through annual tax returns, the treatment of capital gains is somewhat flawed. This is because the wealthy have discretion over when to realize and report their capital gains. Depending on different tax law changes, the capital gains data can be inconsistent from year to year. For example, several capital gains and qualifying dividends tax cuts for the wealthiest 2 percent of households expired in 2013, prompting them to book their capital gains income in 2012 and making the 2013 estimates “too low” (Saez 2015; for details, see Tcherneva 2015). Capital gains, however, are a key component of income for the wealthiest 1 percent of families, worsening income inequality

Table 1 Breakdown of Top Incomes, 2015

Average Real Income	All US Households	Top 10%	Top 5%	Top 1%	Top 0.5%	Top 0.1%	Top 0.01%
Without capital gains	57,281	273,843	404,347	1,053,398	1,621,626	4,502,288	18,862,641
With capital gains	61,920	312,536	477,293	1,363,977	2,193,460	6,747,439	31,616,431

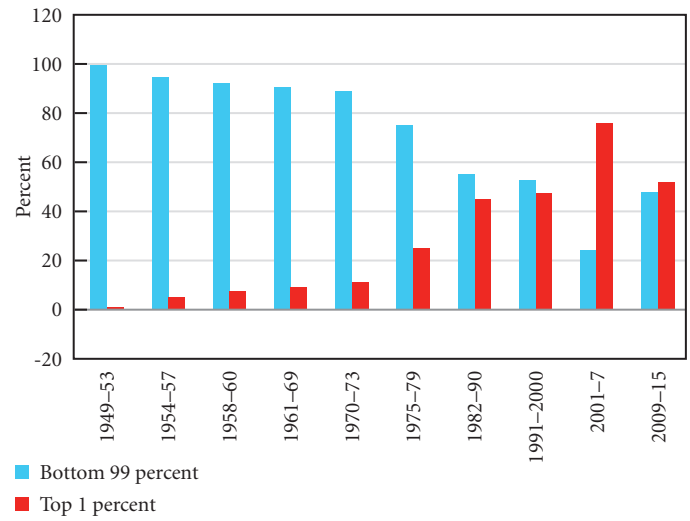
Source: Piketty/Saez 2003, updated 2016

Figure 3 Households' Share of Average Income Growth: 1949–2015 Expansions (excluding capital gains)



Sources: Author's calculations based on Piketty/Saez data and NBER

Figure 4 Households' Share of Average Income Growth: 1949–2015 Expansions (including capital gains)



Sources: Author's calculations based on Piketty/Saez data and NBER

(Figure 4). But even when they are excluded, one can discern significant erosion in the distribution of income (Figure 5).

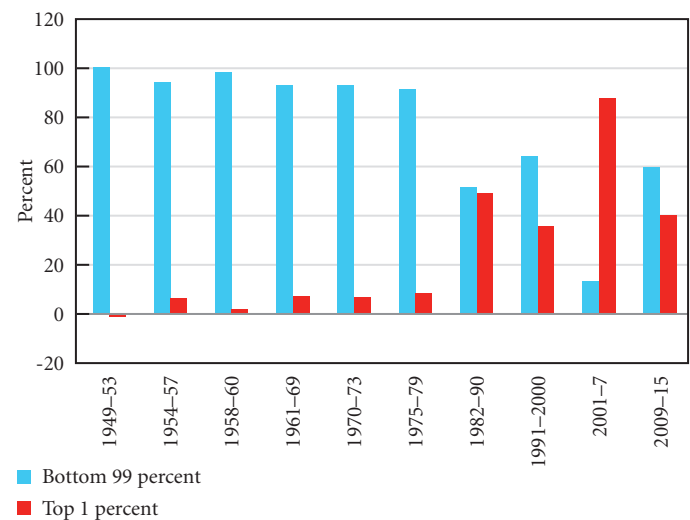
Figures 4 and 5 show that incomes of the bottom 99 percent (with or without capital gains) have recovered more robustly than those of the bottom 90 percent (Figures 2 and 3), meaning that the improvements are primarily concentrated in the next richest 9 percent of families. Their share of income growth is either 30 percent or 38 percent, depending on whether or not one includes capital gains.

Finally, Figure 6 shows how income growth has been distributed over the different business cycles (peak to peak, i.e., including both contractions and expansions). The data for the latest cycle are incomplete, as we are still in it. The graph indicates that in the current cycle, incomes for all groups are still lower than their previous peak in 2007. However, the loss is largely borne by the bottom 90 percent of households.

In sum, the growth pattern that emerged in the '80s and delivered increasing income inequality is alive and well. The rising tide no longer lifts most boats. Instead, the majority of gains go to a very small segment of the population.

As I have discussed elsewhere, this growth pattern is neither accidental nor unavoidable. It is largely a by-product of policy design, specifically, the shift in macroeconomic methods used to stabilize an unstable economy and stimulate economic growth. With respect to how we might begin to reverse these trends, I listed some possibilities:

Figure 5 Households' Share of Average Income Growth: 1949–2015 Expansions (excluding capital gains)

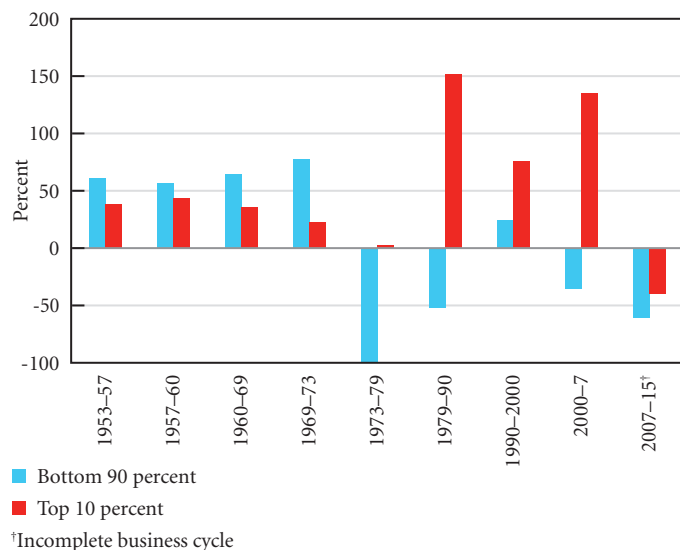


Sources: Author's calculations based on Piketty/Saez data and NBER

A policy orientation that pursues chock-full employment and decent wages can go a long way toward lifting the floor and filling the middle, delivering shared prosperity.

When we look exclusively to the tax system for policy solutions to inequality, we miss this more important piece of the puzzle. Returning to a more equitable variety of capitalism requires far more than just rolling

Figure 6 Households' Share of Average Income Growth: 1953–2015 Business Cycles (including capital gains)



Note: Calculations show peak year to subsequent peak.

Sources: Author's calculations based on Piketty/Saez data and NBER

back regressive tax cuts; it requires resuscitating and modernizing those labor-market-focused policies left behind by the shift to a trickle-down, financial-sector-driven policy regime. Redesigning the tax structure alone will not do the job. Aggressive increases in top marginal tax rates will reduce incomes at the top and thereby improve the income distribution, but more extensive progress will not be made until steps are taken to ensure that incomes at the bottom and the middle rise faster than those at the top. This can be achieved by refocusing policy on labor markets—including a mechanism that links wage increases to productivity gains, prioritizes decent work for decent pay, commits to pay equity, reexamines comparable worth policies, and, importantly, implements an effective employment safety net at living wages for all. These are policies that would ensure that (1) the incomes of the vast majority of people grow rather than shrink in expansions and (2) the majority of the gains from growth go to the majority of families. (Tcherneva 2015, 7)

Note

1. The analysis is based on Piketty and Saez data (2003, updated 2016), which report real average market income before taxes and transfers. Market income includes wages and salaries, entrepreneurial income, dividends, interest income, and capital gains.

References

- Irwin, N. 2014. "The Benefits of Economic Expansions Are Increasingly Going to the Richest Americans." *The New York Times*, September 26.
- Piketty, T., and E. Saez. 2003. "Income Inequality in the United States, 1913–1998." *Quarterly Journal of Economics* 118, no. 1 (February): 1–39. (Tables and Figures updated to 2015 in Excel format, June 2016.)
- Saez, E. 2015. "Striking It Richer: The Evolution of Top Incomes in the United States." (Updated with 2013 preliminary estimates.) Berkeley: University of California. January.
- Tcherneva, P. R. 2014a. "Reorienting Fiscal Policy: A Bottom-Up Approach." *Journal of Post Keynesian Economics* 37, no. 1 (December): 43–66.
- . 2014b. *Growth for Whom?* One-Pager No. 47. Annandale-on-Hudson, N.Y.: Levy Economics Institute of Bard College. October.
- . 2015. *When a Rising Tide Sinks Most Boats: Trends in US Income Inequality*. Policy Note 2015/4. Annandale-on-Hudson, N.Y.: Levy Economics Institute of Bard College. March.